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CHARLES ELMORE CRO

IN THE

Supreme Court of the United States

OCTOBER TERM, 1934

No. 3

SCHUYLKILL TRUST COMPANY
Appellant

v.

THE COMMONWEALTH OF PENNSYLVANIA

Appeal from the Supreme Court of the Commonwealth of Pennsylvania

SUPPLEMENTAL BRIEF FOR APPELLEE

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1934

No. 708

SCHUYLKILL TRUST COMPANY

Appellant

v.

THE COMMONWEALTH OF PENNSYLVANIA

Appeal from the Supreme Court of the Commonwealth of Pennsylvania

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SUPPLEMENTAL BRIEF FOR APPELLEE

At the time of the oral argument in this case, the appellant asked permission to file certified copies of the opinions of the Dauphin County Court in the case of COMMONWEALTH OF PENNSYLVANIA *v.* PROVIDENT TRUST COMPANY, with a memorandum explaining the figures involved in that case.

It is the opinion of the appellee that the appellant has, in its supplemental brief, gone far beyond the authority granted to it by this court with reference to its request and has made certain erroneous and confusing statements with respect to the facts in the Provident Trust Company opinions and also with re-

spect to the principle upon which the Commonwealth relies in certain cases cited by it which the appellee believes should be corrected. It was due to this fact, considering the importance of this case, that the appellee requested and obtained permission to file this supplemental brief.

On page 2½ of the supplemental brief for appellant, it is stated

> "It is submitted that an analysis of this opinion demonstrates the fact that the reasoning, which is the basis of the judgment of the Dauphin County Court, Judge Hargest's theory of the settlement and his mathematical calculations made in the application of his theory contradict expressly the conclusions of the state supreme court in the instant case, to wit, that the tax is a tax upon shares qua shares and therefore United States obligations, Philippine Islands bonds, Joint Stock Land Bank bonds, National Bank shares and Federal Reserve Bank stock are not taxed, are not made the basis of a tax, are not discriminated against and that therefore the state has authority to tax the shares of stock issued by trust companies owned by nonresidents of the state."

and appellant also states on page 10 of its supplemental brief:

> "In deducting assets made tax-free by the statute so as not to tax them the state courts construed and applied the statute as imposing a tax upon assets of the trust company * * *".

This is not correct for the reason that nowhere in the opinion of the Dauphin County Court is the statement, nor can it be inferred from the court's reasoning that the tax in question is not a tax on shares qua shares,

but on the contrary, we refer this court to the language of the court in its opinion (40 Dauphin County Reports, page 163) where the court said:

> "It is settled that the tax imposed upon the shares of a trust company is a tax upon the shares held by the shareholders and is not a personal property tax nor a tax on the assets of the trust company. Commonwealth *v.* Schuylkill Trust Company, 38 Dauphin, 22; 315 Pa. 429; * * *"

and further in the opinion upon the exceptions (41 Dauphin Court Reports, page 4) where the court said:

> "It must be kept in mind that the thing to be accomplished is the taxation of the shares of stock at actual value. Who are to be taxed? The stockholders. The thing to be taxed is what the stockholders own. * * *"

On page 4 of the supplemental brief for appellant, the appellant, after having stated the questions involved at page 3, and referring particularly to question number two (whether the defendant is entitled to a flat or only a proportionate deduction from the value of its shares in investments in capital stock of a Pennsylvania title company, the shares of a national bank and the capital stock of Pennsylvania corporations all paying a capital stock tax or tax on shares) the appellant stated:

> "The court answered the second question by holding that some assets of the trust company were entitled to be deducted 'flat' and others 'proportionately' from the amount of the capital stock paid in, surplus and undivided profits (pp. 159-162) because such assets were included within the class of assets exempted under the language of

> the statute, to wit, 'shares of stock of corporations liable to pay to the Commonwealth a capital stock tax, or relieved from the payment of capital stock tax or tax on shares' * * *"

and it further states at page 6:

> "The significance of the 'proportionate' method of settlement outlined and applied in this case as over against that applied in the case of the Schuylkill Trust Company, the instant appellant, lies in the factors included within and excluded from the numerator and denominator of the fraction and the multiplicand to which the fraction was applied. In the Schuylkill Trust Company case the numerator of the fraction was the actual value of the capital stock, surplus and undivided profits of the trust company; the denominator was the actual value of the total assets in which were included the total value of the shares of stock which are exempt under the language of the statute as well as the value of the non-taxable assets consisting of United States securities, Philippine Islands bonds, Joint Stock Land Bank bonds and National Bank shares. By reason of the increase of the denominator of the fraction by the inclusion of such exempt and non-taxable assets, the application of the fraction and the formula in determining the amount deducted from the capital stock, surplus and undivided profits in order to determine the taxable value resulted in a lessening in the amount of the deductions and a consequent increase of tax liability (R. 14-17)."

These statements are both erroneous and confusing. The appellant does not inform this court that the reason that certain deductions were made "flat" and others "proportionately" was not only because such assets were included within the class of assets ex-

empted under the language of the statute, but, in addition to this fact, because the court found that upon proof offered, the assets permitted to be deducted "flat" were purchased out of capital stock paid in, surplus and undivided profits, whereas in the absence of proof that the investments were purchased out of capital stock paid in, surplus and undivided profits a proportionate deduction was only allowed for such investments.

The submission of proof of the purchase of certain investments as described in the taxing statute out of capital stock paid in, surplus and undivided profits and the finding of this fact by the court was the basis for the allowance of a flat deduction for such investments in the Provident Trust Company case, and the appellant makes this admission on page 10 of its supplemental brief. In the instant case, the Schuylkill Trust Company did not offer proof showing the purchase of any of its investments out of capital stock paid in, surplus and undivided profits and it was because of this fact, and the court so found, that only a proportionate deduction was allowed for the investments of the trust company and not a flat deduction; the court saying in its opinion at R. page 50:

> "The defendant did not prove that it had purchased these stocks out of capital paid in, surplus and undivided profits. It may have been very difficult or impossible for the defendant to unscramble depositors' money from the capital stock account and show from which the stock was purchased. This, however, is entirely a matter for the defendant. The defendant not having proven its purchase of these stocks out of capital, surplus, and undivided profits, the Commonwealth might

> have refused to allow any deduction whatever, but instead it pursued the more equitable course, as was also done in the Hazelwood Savings & Trust Co. case." (271 Pa. 375)

The presence of proof of the purchase of certain shares of stock out of capital stock paid in, surplus and undivided profits in the Provident Trust Company case and the absence of proof of the purchase of certain shares of stock out of capital stock paid in, surplus and undivided profits in the instant case accounts for the difference in the factors included within and excluded from the numerator and denominator of the apportionment fraction used in each of these cases.

The appellant cannot complain because of the large deduction in the Provident Trust Company case when the deduction in the instant case is based upon the failure of the appellant to prove its right to a greater deduction.

On page 7 of the supplemental brief of the appellant, it is stated in discussing the deduction in the Provident Trust Company case:

> "The deduction was allowed in the amount of $6,616,754. in accordance with the court's construction and application of the provisions of the statute which exempted the class of assets described as (1) shares of stock of corporations liable to pay to the Commonwealth a capital stock tax or tax on shares and (2) shares of stock of corporations relieved from the payment to the Commonwealth of a capital stock tax or tax on shares. * * *"

This is not correct. The only deduction which was permitted "flat" or "proportionately" in the Provident Trust Company case was for shares of stock upon which a capital stock tax or a tax on shares had been paid. Shares of stock of manufacturing corporations relieved from the payment to the Commonwealth of a capital stock tax were not involved in that case because there were no such shares owned by the Provident Trust Company.

At the oral argument in the instant case before this court, the impression was created that shares of stock of manufacturing corporations relieved from the payment of a capital stock tax had been deducted. We call to the attention of this court that in the instant case, the question of deduction of shares of stock of manufacturing corporations relieved from the payment of capital stock tax was not involved because the Schuylkill Trust Company did not own any such shares, and therefore, we believe that such an impression, if existing, should be corrected. The only deduction allowed in the instant case was the deduction of shares of stock of corporations upon which a capital stock tax or tax on shares had been paid.

On page 16½ of the supplemental brief of the appellant it is stated that

> "* * * He (lower court Judge) held that the 9276 non-taxable Federal Reserve Bank shares were to be deducted 'flat' irrespective of whether or not they were a part of the capital structure of the trust company or purchased from its general fund. He had found as a fact that 5076 of the said total of 9276 shares had been purchased out of the general funds of the Provident Trust Company. (See certified copy of first opinion, p.

239a, par. 5; 40 Dauphin County Reports, p. 162, par. 5)."

As stated by the appellant the statement above referred to is both incorrect and confusing. Nowhere in the opinion of the lower court in the Provident Trust Company case does the court hold that the Federal Reserve Bank shares were to be deducted irrespective of whether or not they were a part of the capital structure of the trust company or purchased from its general fund. This is merely a deduction made by the appellant.

It is true that the lower court judge in the Provident Trust Company case did allow a flat deduction for investment in shares of stock of the Federal Reserve Bank from capital stock paid in, surplus and undivided profits, but we submit that in view of the following language used by the lower court judge in his opinion, to wit:

> "'We are, therefore, of opinion that we must reverse our former conclusion and now hold that this language prevents the taxation of so much of the shares of the defendant company as is invested in the stock of corporations which are relieved from the payment of a capital stock tax either because of some provision of an act of assembly or because they are beyond the power of the State to tax.'"

the allowance of a flat deduction for investment in Federal Reserve Bank shares was erroneous for the reason that such deduction was based upon the construction of the word "relieved" appearing in the taxing statute and upon the court's failure to require and consider upon the submission of proper proof

whether Federal Reserve Bank shares had been purchased out of capital stock paid in, surplus and undivided profits, as the court in the same case did require and consider proof of the purchase of national bank shares out of capital stock paid in, surplus and undivided profits allowing only a proportionate deduction for 150 shares of the Central National Bank and a flat deduction for 300 shares because the Provident Trust Company did not prove that the 150 shares had been purchased out of capital stock paid in, surplus and undivided profits.

It is the position of the Commonwealth that a "flat" deduction should be allowed under the taxing statute only where adequate proof is offered to show the purchase of investments out of capital stock paid in, surplus and undivided profits and that a proportionate deduction should be allowed for investments in the absence of such proof. We submit that this position of the Commonwealth is supported by the courts of the Commonwealth of Pennsylvania in the opinions in the Provident Trust Company case and in the opinions in the instant case and is recognized by the Justices of this Court in the dissenting opinion in the case of BANK OF CALIFORNIA NATIONAL ASSOCIATION *v.* RICHARDSON, 248 U. S. 476 (1919). Therefore, it is the Commonwealth's contention that the allowance of a proportionate deduction in the instant case for ownership by the Schuylkill Trust Company of shares of stock of the Philadelphia National Bank is proper and that the allowance of a flat deduction for ownership of Federal Reserve Bank shares by the lower court in the Provident Trust Company case was erroneous.

In order to clear up any possible confusion arising by reason of the discussion by the appellant in its supplemental brief, of the original opinion and the opinion upon the exceptions in the Provident Trust Company case, we wish to direct the court's attention to the fact that the sole effect of the opinion of the court upon the exceptions in the Provident Trust Company case as discussed by the appellant in its supplemental brief was to determine the method of arriving at the amount of deduction to be allowed for investment by the trust company in shares of stock of corporations owned by the trust company and upon which a tax had been paid. We submit, therefore, that the opinions of the lower court in the Provident Trust Company case on this point can have no bearing upon the Federal questions involved in the instant case.

On page 18½ of the supplemental brief for the appellant, the statement is made that

> "None of these cases (Commercial Bank *v.* Chambers, 182 U. S. 556 (1901), Amoskeag Savings Bank *v.* Purdy, 231 U. S. 373 (1913) and Bank of California National Association *v.* Richardson, 248 U. S. 476 (1919) are cited in support of a contention 'that in order to constitute a valid tax on shares of bank stock in the hands of shareholders, the tax need not be upon the shareholders' entire interest') sustains the contention in support of which they are cited by the Commonwealth. * * *"

We merely direct this court's attention to this portion of appellant's supplemental brief to show that appellant offers nothing in support of this statement. We submit that these cases do substantiate the principle for which they were cited.

The Commonwealth contends that the important question in this case is whether the Act of 1907, as amended, imposes a tax on the shareholders interest or a tax on the capital structure of the bank.

The appellate courts of Pennsylvania have, in many cases, cited in the original brief of the appellee and in the instant case decided that the tax in question is a tax on shares qua shares. The fact that deductions are permitted to shareholders by the taxing statute does not change the nature of the tax from a tax on shares in the hands of the shareholders to a tax on the corporation.

COMMERCIAL BANK *v.* CHAMBERS, 182 U. S. 556 (1901)

AMOSKEAG SAVINGS BANK *v.* PURDY, 231 U. S. 373 (1913)

BANK OF CALIFORNIA NATIONAL ASSOCIATION *v.* RICHARDSON 248 U. S. 476, (1919)

In these cases, this court has upheld the deduction to the shareholder of something which has been taxed to the bank. **In the instant case, the only deduction allowed has been that for shares which have paid a capital stock tax or a tax on shares.** Even if in the instant case a deduction had been permitted for shares of stock of corporations which had been relieved from the payment of a capital stock tax or tax on shares, how can it be said that the allowance of such an additional deduction changes the nature of the tax from a tax on shares to a tax on the corporation? This court has recognized that "the theory that shares in corpora-

tions are property entirely distinct and independent from the property of the corporation" and that "the tax on an individual in respect to his shares in a corporation is not regarded as a tax upon the corporation itself" and has so held in the following cases:

CLEVELAND TRUST COMPANY *v.* LANDER, 184 U. S. 111 (1902)

HOME SAVINGS BANK *v.* DES MOINES, 205 U. S. 503.

If the tax in the instant case is a tax on shares, there is no discrimination against United States securities owned by the bank by reason of the allowance of deduction to the shareholders of the bank for shares of stock of corporations which have paid a capital stock tax or tax on shares because of the theory of distinction between the interest of the shareholder and the interest of the corporation; and for the further reason that under this theory we are not concerned with what assets of the bank go to make up the capital stock, surplus and undivided profits used as the measure of the value of the shares of the bank to be taxed to the shareholders.

We, therefore, respectfully submit that the judgment of the court below should be affirmed.

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